RATING REPORT

Orient Textile Mills Limited (OTML)

REPORT DATE:
December 23, 2021

RATING ANALYST:

Asfia Aziz
asfia.aziz@vis.com.pk

Muhammad Taha
m.tahi@vis.com.pk

RATING DETAILS		
Rating Category	**Initial Rating**	
	Long-term	**Short-term**
Entity	BBB	A-2
Rating Outlook	Stable	
Rating Date	December 23, 2021	
Rating Action	Initial	

COMPANY INFORMATION	
Incorporated in 1986	**External auditors:** Kreston Hyder Bhimji & Co.
Public Unlisted Company	**CEO:** Mr. Rafiq Ebrahim
Key Shareholders (with stake 5% or more):	
Mr. Ahmed – 5.9%	
Ms. Muddassir – 5.52%	
Mr. Mohsin – 5.52%	
Mr. Rafiq – 9.32%	
Miss Afsheen – 22.17%	
Mr. Ismail – 7.45%	
Mr. Amjad – 5.52%	
Miss Anum – 5.43%	
Mr. Karim – 7.36%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria Methodology – Industrial Corporates (August 2021) **https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf**

Orient Textile Mills Limited (OTML)

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Orient Textile Mills Limited (OTML) was incorporated as an unlisted public Company in 1986. The shares of the Company are owned by family members. Principal activity of the company includes manufacturing and sale of textile and related products particularly in home-textile.

Financial Statements of the company for FY21 were audited by Kreston Bhimji & Co. which lie in Category A of the SBP Panel of Auditors.

Profile of the CEO

Mr. Rafiq Ebrahim has been recently appointed as CEO in Orient Textile and Ebrahim Textile after the sad demise of his elder brother Late Iqbal Ebrahim. Mr. Rafiq has vast experience of over 44 years in dealings with overall operations of the textile process, and marketing of textile products both in local markets and international markets. Due to his extra ordinary understanding of composite textile business operations he earned his name in the world of textile internationally also. Previously, he was working as Senior Director Operations & Marketing for domestic but now supervising the entire operations of Group's Textile businesses.

Orient Textile Mills Limited (OTML) is one of the two textile companies owned by Ebrahim Group of Companies, which was incorporated in 1986 and is headquartered in Karachi. The group owns business interest in Textile (Ebrahim Textiles), Dairy Products (IGLOO) and Beverage Industry (Imran Crow Corks).

Group Snapshot
Orient Textile Mills (Weaving)
Ebrahim Textile Mills (Textile processing)
Imran Crown Corks (Crown and Plastic Closures)
Pakistan Dairy Products (Dairy Products)

The company mainly focuses weaving of griege cloth and sale of home textile products, such as sofa cloths, curtains, bedsheets, and comforters. In addition, it offers weaving services to local clients. All processing for their export sales is carried through related concern, Ebrahim Textiles. Exports customers are primarily in Europe and USA The power requirement of the company is met via internal generation (gas based generators), as no sanctioned load from KE is available. Manufacturing unit is situated at Landhi Industrial Area across a 9 acres land space.

Product Portfolio
Greige Cloth
Bedsheets/Curtains/Sofa Covers/Comforters

Capacity Utilization

	FY19	FY20	FY21
Installed capacity for weaving (picks in millions)	146	163	163
Actual utilization (picks in millions)	138	149	153
Capacity Utilization (%)	**94.5%**	**91%**	**94%**

At end-FY21, the capacity of the entity was 3m meters per month, with a utilization level of over 90% consistently on a timeline basis. At present, there are 248 looms installed at the facility, out of which 56 are jacquard looms, about 140 are plain looms, and the rest are Dobby looms.

The company initiated BMR initiatives in 2015 that has been completed at end-Sep'21. As part of the same, older looms were replaced air jet looms that offered higher rotation speeds of aiding in enhancement of overall installed capacity of the plant. In the medium-term, the company has no expansion plans on board.

<u>Key Rating Drivers</u>

Recovery in industry wide exports post ease in COVID-19 lockdown measures support business risk profile of the company.

- Subsequent to posting export contraction in FY20 - owing to the pandemic-induced slowdown experienced in H2'FY20 – Pakistan's export base grew by 14% in FY21, which is partly attributable to a low base effect. Pakistan's export proceeds have oscillated in the range of USD 22-25b during the past decade (FY11-FY21). So the uptick is largely aligned with historical numbers and is not considered material.
- Share of textile exports in total exports has oscillated in the range of 54-59%, coming in at 57% during the past 2-years (FY20-21). In FY21, owing to the similar low-base effect, as discussed above, textile exports were up 13%.
- In USD' terms textile exports have grown at a CAGR of 4.4% during the past 3-year period (FY19-FY21), despite depreciation in average USD/PKR parity of 24%, 16%, and 1% in FY19, FY20 and FY21 respectively.
- As illustrated in the table above, textile exports in Q1'FY22 were 37% higher than SPLY. Inclusive of textile exports for Oct'2021, the number for 4M'FY22 textile exports came in at USD 6b. With additional capacities coming online in January 2022, textile exports for FY22 are likely to exceed the annualized figure of USD 18b.
- As illustrated in the table below, the composition of textile exports has depicted improvement in the last 4-yar period, with contribution from higher value added segment increasing from 72.9% in FY18 to 80.7% in FY21 of aggregate textile exports.
- Cotton production in Pakistan, on the other hand, was at its lowest level in decades for FY21. Cotton prices rose to a new 11-year high of ~Rs. 13,000/maund as a result of the production shortage, and cotton imports have climbed by 59.8% in quantity and 68.1% in USD terms, for FY21 vis-à-vis preceding year.
- Given favorable weather conditions, cotton production in Pakistan posted strong growth in FY22, with cotton crop for Jul-Nov'22 (Rabi) season being 81% higher than SPLY. Nevertheless, the upward momentum in cotton pricing continued in FY22, with prices as of November 2022 hovering at ~Rs. 16,000 per mound.
- The margins of textile operators have broadly depicted improvement despite the uptick in raw material costs, given that the same was offset by exchange rate movement. Nevertheless, higher raw material pricing has increased the working capital requirements for textile operators, which is likely to weigh on the liquidity of textile players. VIS expects the order book for the industry to remain adequate in the ongoing year along with transfer orders of neighboring countries, easing our business risk concerns

Topline of the company has grown at a CAGR of 27% over the last three years. During FY21, a sizeable increase of 47% was reported led by ease in Covid-19 restrictions and revival of economic activity in the country. This was further aided by the completion of BMR project that enhanced overall capacity levels of the company. Going forward, escalation in sales revenue is projected on the back of gradual economic recovery worldwide.

Sales revenue of the company rose by around 47% during FY21 and was reported at Rs. 6.7b (FY20: Rs. 4.6b, FY19: Rs.3.9b). Growth in topline was largely a function of higher volumetric sales in the international market with a 10-15% increase contributed by higher prices due to currency devaluation. In addition to that, the company capitalized on the opportunity presented by the pandemic and manufactured face masks and bed sheets for hospitals, products that are not part of the main portfolio. Proportion of exports sales in the total sales mix have been increasing over the past two years with the same being reported at 87% (FY20: 79%, FY19: 73%) during FY21. Key focus of the company remains towards international clients. Geographic concentration risk in exports sales is considered manageable, as the customers are spread across Europe and the USA. Client wise concentration risk is considered to be on the higher side; however comfort is drawn from long-term relationships with major clients. Management expects growth momentum in sales to continue going forward, as the economies continue to recover from the Covid-19 pandemic and the company establishes its planned diversification in the client base.

Margins depict a declining trend on a timeline basis.

Gross margin (GMs) of the company declined to 6.5% during FY21 (FY20: 7.9%, FY19: 9.8%) being a function of higher cost of raw material procured with yarn prices reporting an increase of around 35-40% in the outgoing year due to currency devaluation and demand-supply dynamics in the local market. Around 40% of the raw material purchases comprise imported yarn. Higher overall operating expenses encompasses greater commission and costs on exports sales, net exchange loss and one-off loss on disposal of fixed assets to the tune of Rs. 58m, Rs. 23m and Rs. 32m, respectively. Finance charges also depicted an increase of Rs. 56.5m owing to expansion-led elevated debt levels at Rs. 3.8b (FY20: Rs. 2.2b, FY19: Rs. 1.7b). Overall profitability of the company was supported by higher other income provided by one-off reversal of provision of GIDC and re-measurement gain on discounting of GIDC provision. Going forward, while the company projects improvement in revenues and margins on the back of higher prices and devaluation, we expect net profitability to remain under pressure on account of increased gearing.

Cash flow coverages against outstanding obligations have reduced over the past two years due to increase in debt levels to finance BMR and working capital requirements. Ratings are dependent on further improvement in liquidity indicators, going forward.

In absolute terms, Funds from Operations (FFO) reduced to Rs. 324m (FY20: Rs. 371m, FY19: Rs. 385m) on account of lower profitability during FY21. Debt Service Coverage Ratio (DSCR) is considered satisfactory being reported at 2.51x (FY20: 2.56x, FY19: 2.92x). FFO/Long-Term Debt and FFO/ Total Debt both declined to 17% (FY20: 31%, FY19: 49%), and 8% (FY20: 17%, FY19:

22%) at end-June'21, respectively. Inventory and trade debts provide sufficient coverage for short-term debt obligations, while current ratio was reported at a reasonable level of 1.3x at end-June'21. Going forward, projected improvement in profitability and gradual debt repayment is expected to bode well for liquidity indicators.

Leverage indicators have surged on a timeline basis due to elevated debt levels to finance working capital needs and BMR expansion. Going forward, leverage indicators are expected to improve due to gradual repayment of long term debt.

Equity base of the company increased to Rs. 1.1b (FY20: Rs. 0.9b FY19: Rs. 0.69b) on account of profit retention and equity injection of Rs. 131m in the form of long-term loan offered by a related party. Quantum of total debt increased to Rs. 4b (FY20: Rs. 2.1b; FY19: Rs. 1.7b) at the end of FY21 to finance working capital requirements and BMR expansion. Resultantly, gearing and leverage ratios were reported higher at 3.4x (FY20: 2.4x; FY19: 2.5x) and 4.8x (FY20: 4.3x; FY19: 4.2x), respectively at end-June'21. Given export-oriented operations, debt composition of the company comprises lower rate financing arrangements provided by the GoP including LTFF, TERF and ERF. The management does not expect further drawdown of long-term debt in the medium term. However, with increasing business needs, working capital requirement may increase. Total available running finance facilities available to the company was Rs. 2.6b at end-June'21. Going forward, leverage indicators are expected to improve due to gradual repayment of long term debt. Ratings are underpinned with projected improvement in leverage indicators going forward.

Corporate Governance Structure depicts room for improvement

Given status of a public unquoted company, room for improvement exists in the corporate governance structure. The Board is represented by seven directors comprising family members. Each one of them is responsible for a specific function or business unit in the entity. As such, risk of succession is fairly mitigated.

The company plans to implement Oracle EBS entity wide, starting in Jan 2022 under agreement with A.F. Ferguson and Co.

Financial Summary (Rs. in m)				
Balance Sheet	**FY18**	**FY19**	**FY20**	**FY21**
PPE	1,088	1,204	1,468	1,989
Long Term Investments	-	9	-	-
Stock-in-Trade	901	1,310	1,575	3,005
Trade Debts	533	656	948	659
Cash & Bank Balances	26	46	13	20
Total Assets	2,828	3,567	4,803	6,581
Trade and Other Payables	614	1,013	1,595	1,214
Long Term Debt	536	778	1,207	1,935
Short Term Debt	1,070	958	947	1,924
Total Debt	1,607	1,736	2,154	3,860
Paid Up Capital	405	405	405	405
Total Equity	514	687	908	1,141
Income Statement				
Net Revenue	3,309	3,847	4,584	6,716
Gross Profit	311	375	360	436
Profit Before Tax	75	127	137	121
Profit After Tax	51	95	176	104
Ratio Analysis				
Gross Margin (%)	9.4%	9.8%	7.9%	6.5%
Net Margin (%)	1.6%	2.5%	3.8%	1.5%
Net Working Capital	(66)	245	702	992
FFO	210	385	371	324
FFO to Total Debt (%)	13%	22%	17%	8%
FFO to Long Term Debt (%)	39%	49%	31%	17%
Debt Servicing Coverage Ratio (%)	3.55	2.92	2.56	2.51
Gearing (x)	3.13	2.53	2.37	3.38
Leverage (x)	4.51	4.19	4.29	4.77
Current Ratio (x)	0.96	1.12	1.27	1.28
STD Coverage (%)	134%	205%	267%	190%
ROAA (%)	2%	3%	4%	2%
ROAE (%)	10%	16%	22%	10%

ISSUE/ISSUER RATING SCALE &DEFINITIONS Appendix II

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES — Appendix III

Name of Rated Entity	Orient Textile Mills Limited
Sector	Textiles
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	see table below
Instrument Structure	N/A
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile. Copyright 2021 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
Dec 23, 2021	BBB	A-2	Stable	Initial

Due Diligence Meetings Conducted

Name	Designation	Date
Saleem Aziz	CFO	2-Nov-21
Muhammad Jahangir	Senior Manager Finance & Taxation	2-Nov-21
Ali Shayan	AM Accounts & Finance	2-Nov-21
Zohaib Hassan	DM Accounts & Purchase	2-Nov-21